

**Initial Statement of Reasons
Overview/Non-Controlling Summary**

PROPOSED REGULATION 1668, SALES FOR RESALE

Regulation 1668 is proposed to be revised to clarify the documentation requirements of a qualified resale certificate and purchase order used to support a sale for resale.

Specific Purpose

The purpose of the proposed regulation is to interpret, implement, and make specific Revenue and Taxation Code sections 6091 and 6241, which presume that all sales are retail sales until the seller proves the contrary. This regulation is necessary to provide guidance to taxpayers affected by this statute.

Factual Basis

Regulation 1668, *Resale Certificates*, implements Revenue and Taxation Code sections 6091 and 6241, which presume that all sales are retail sales until the seller proves the contrary. The seller can overcome this presumption by taking from the purchaser a resale certificate as provided in Regulation 1668. A document is regarded as a resale certificate if it contains all the essential elements specified in 1668(b)(1). When the seller takes a timely resale certificate in good faith from a person who holds a valid California seller's permit, the seller is relieved from liability for sales tax and the duty of collecting use tax. If the purchaser thereafter uses the property rather than reselling it, the purchaser is responsible for payment of any tax due. If a purchaser who gives a resale certificate for property makes any storage or use of the property other than retention, demonstration, or display while holding it for sale in the regular course of business, the tax must be reported and paid by the purchaser. Subdivision (b)(4) of Regulation 1668, which explains the use of a qualified resale certificate, provides that if a purchaser wishes to designate on each purchase order whether the property being purchased is for resale, the seller should obtain a resale certificate that states "see purchase order" in the space provided for a description of the property to be purchased. Each purchase order must then specify whether the property covered by the order is purchased for resale or subject to tax. If each purchase order does not so specify, or is not issued timely, it will be assumed that the property covered by that purchase order was not purchased for resale, and the sale or purchase is subject to tax. If the purchase order is issued for property some of which is to be resold and some to be used, the purchase order must specify which items are purchased for resale and which items are not purchased for resale. In order to support a sale for resale, a seller must retain the purchase order in conjunction with the original qualified resale certificate.

This issue was referred to the Board's Business Taxes Committee (BTC) to clarify whether a sale for resale is valid when the instructions on the resale certificate state "see purchase order" and the purchase order identifies the property is being purchased for resale by using terminology such as "not taxable" or "taxable: no" as opposed to "for resale." If valid and accepted in good faith, the seller accepting the purchase order combined with a qualified resale certificate will be

relieved from the liability for tax if the transaction is later found to be taxable and the liability to pay the tax will rest with the purchaser. In July 2008, Board staff was instructed by memo that the provisions of subdivision (b)(4) of Regulation 1668 require that a purchase order issued in support of a qualified resale certificate is valid and relieves the seller from the liability for tax only if the purchase order includes the phrase “for resale.” In response to such interpretation, a number of taxpayer representatives and consultants (hereafter referred to as “interested parties”) objected to this policy and questioned whether Board staff consistently followed such interpretation in the past. Interested parties organized meetings with representatives from the Board’s Sales and Use Tax Department and Board Members’ offices to discuss this issue. As a result, the BTC Chair referred this matter to the BTC for analysis and recommendation. Staff met with interested parties on November 25, 2008, to discuss proposed revisions to the regulation and agreed to incorporate additional revisions suggested by the interested parties to bring consensus to the proposal.

The proposed regulatory changes amend subdivision (b)(4) of Regulation 1668 to provide that the acceptable resale designation on a purchase order is not limited to the phrase “for resale” and may include comparable terminology, such as “resale = yes,” “nontaxable,” “taxable = no,” or similar terminology on a purchase order, indicating that tax or tax reimbursement should not be added to the sales invoice and will be regarded as designating that the property described is purchased for resale provided the combination of the purchase order and the qualified resale certificate contains all the essential elements provided in subdivision (b)(1). The proposed regulatory changes also provide that a purchase order where the applicable amount of tax is shown as \$0 or is left blank will not be accepted as designating that the property is purchased for resale, unless the purchase order also includes the phrase “for resale” or other terminology described above to specify that the property is purchased for resale.

Pursuant to Government Code section 11346.5(a)(8), the Board of Equalization finds that the adoption of the proposed regulation will not have a significant adverse economic impact on private businesses or persons. The regulation is proposed to interpret, implement, and make specific the authorizing statutes. These changes will clarify the interpretation or administration of the sales and use tax laws. Therefore, the Board has determined that these changes will not have a significant adverse economic impact on private businesses or persons.